Deloitte appreciates the opportunity to provide comments on the Financial Accounting Standards Board’s (“FASB”) Invitation to Comment (“ITC”), Agenda Consultation.

We applaud the Board for soliciting feedback about financial reporting issues that it should consider adding to its agenda. This is an important step in gaining constituent input on the most vexing issues and commitment to the future path for standard setting. We agree now is the time to consider what new major projects the Board should undertake. While constituents will be busy over the next few years implementing recently issued major standards, we would expect that all of the issues noted in the ITC will take years to complete and not result in final standards until after implementation of the recently issued standards is complete.

All of the topics included in the ITC have merit for being added to the agenda. While we do not think that the standards related to these topics are so flawed that they provide misleading financial information, they are areas with some of the most difficult issues and could be improved. However, since the Board’s resources are finite, priorities must be set. Therefore, we believe that only two of the four proposed topics should be added to the Board’s current agenda. Too many major projects on the Board’s agenda at the same time could dilute its resources and focus, in which case it could need additional time to complete projects and may not implement the best solutions.

Further, the additions to the agenda should not replace the current significant projects such as disclosure effectiveness and conceptual framework which we encourage the Board to continue working on and complete. The addition of the proposed topics also should not prevent the Board from taking on narrow projects as the need arises and provide support for the implementation of the recently issued major ASUs (e.g., on revenue recognition, leases, and financial instruments).

We believe that the two topics the FASB should add to its agenda are (1) distinguishing liabilities from equity and (2) reporting performance and cash flows.
In addition, we think that these two topics are related to some extent, since changes to performance reporting may be the key to differentiating claims on assets. For these projects to be successful, solutions should be rooted in broad concepts in order to be viable for a long period of time and to avoid contradictions with other standards. In addition, the Board should continue to use the project management steps it has instituted, including an extensive research phase for identifying root issues. Also, the Board’s latest innovation of more extensive education sessions to identify all the issues and how they interact before any decisions are made, appears to be helpful, provided there is full transparency around decisions giving constituents a chance to react and provide feedback.

Distinguishing Liabilities from Equity

The current guidance on this topic is overly complex and prone to misunderstanding by preparers, practitioners, and other stakeholders. This continues to be an area of frequent misapplication leading to numerous restatements. The existing guidance includes too many competing models that are rules-based and form-driven, which result in instruments that have economically similar characteristics being accounted for in different ways.

A primary purpose for differentiating liabilities from equity under the current regime is that changes in liabilities are recognized in an entity’s performance (i.e., comprehensive income) whereas changes in equity are not. The current definition of a liability in the conceptual framework, while worthy of improvement, is fairly understandable. However, the guidance in current standards is not always consistent with this definition. For example, under current standards certain instruments that do not meet the current definition of a liability must be classified as liabilities because better financial information is conveyed by requiring entities to recognize the changes in these instruments in comprehensive income. An additional complication is that a reporting entity may enter into transactions that are settled in the entity’s shares but have no relationship with ownership. That is, an entity can use its shares similarly to a currency as payment for transactions indexed to various market factors.

One solution could be to revise the definition of a liability to encompass more than the characteristics of form of settlement (i.e., more than a sacrifice of assets from the reporting entity’s perspective) and timing of settlement (i.e., the sacrifice occurs before liquidation of the reporting entity). Another approach could be to define equity and make liabilities the residual.

However, we think a better approach would be to challenge the notion that changes in all equity instruments should not be recognized in comprehensive income. This approach would largely retain the current definition of a liability (subject to potential improvements in clarification). We believe it is useful to retain a classification for instruments with an obligation to sacrifice assets prior to liquidation. However, for instruments that do not meet the definition of a liability, we believe that a distinction should be made between owners’ equity and non-owners’ equity. Thus, all claims on an entity’s assets would be shown in one of three categories within the statement of financial position: (1) liabilities, (2) non-owners’ equity, or (3) owners’ equity.
The conceptual framework refers to owners of an entity and equity in ways that do not appear to be exactly synonymous. Equity is defined as the residual interest after deducting liabilities from assets. Owners are referred to in various passages including comprehensive income. Comprehensive income is a broad measure of transactions and other events, including changes in equity except investments by owners and distributions to owners. Thus, there appears to be a basis to differentiate non-owners’ equity from owners’ equity.

While both classes would represent instruments that do not contain an obligation to sacrifice assets before an entity’s liquidation, only changes in non-owners’ equity (which would be subject to remeasurement) should be recognized in comprehensive income such that total comprehensive income represents the residual accruing to owners. (See our comments below on performance reporting which proposes that certain changes in non-owners’ equity be presented in a separate section within comprehensive income.) The changes in value accruing to non-owners presented in comprehensive income should provide useful information to owners. While we advocate remeasurement of non-owners’ equity, this does not mean these instruments must be measured at fair value for all periods; the most appropriate measure is an area in need of further analysis.

In order to differentiate owners’ equity from non-owners’ equity, a definition of owners’ equity will be necessary. One potential definition could encompass that the characteristics of owners’ equity include (1) a substantial initial net investment in an issued instrument of the entity (one that does not meet the definition of a liability) and (2) no obligation for the reporting entity to settle this instrument, except when the entity is liquidated (i.e., a perpetual instrument). Examples of instruments that would have these characteristics would be perpetual, non-redeemable common stock and preferred stock. Common examples of non-owners’ equity would be equity derivatives (provided that they do not meet the definition of a liability) such as warrants, purchased/written call options, and forwards to sell stock.

Although we believe that these characteristics would be sufficient, if a narrower definition of owners’ equity is desired, additional potential characteristics could be that (1) the instrument must provide participating rights (i.e., the ability to participate in the decisions that most significantly affect the entity’s performance, such as voting for the board of directors) and (2) the variability of return on the instrument is directly related to the entity’s operating performance (i.e., these criteria may eliminate many preferred stock instruments with a stated fixed dividend and fixed return upon liquidation). Another variation may be to treat as owners’ equity, where an entity would otherwise not have any owners’ equity, redeemable shares with the lowest priority.

Under this proposed model, a complication that would need to be addressed is the treatment of compound instruments. These are instruments that combine multiple instruments as indicated by having two or more settlement alternatives with different values. For example, convertible debt combines a liability, which is settled in cash on the basis of a return of principal and interest, and an option to acquire common stock providing a different value. Thus, compound instruments combine instruments from two of the categories of liabilities, non-owners’ equity, and owners’ equity. This model proposes that such instruments be separated into their components. Although the definition of a component may be similar to the current definition of an embedded
derivative, we would support research and evaluation related to how to define a component that would need to be presented separately and would expect more “bifurcation” of separate components than under current guidance. Such a model would address the issues in current GAAP under which instruments with similar characteristics and risks are accounted for differently on the basis of the structure of the instrument (e.g., depending on whether the feature or option is freestanding or embedded). At inception of the compound instrument, the value of each component would first be assigned to liabilities, then to non-owners’ equity, with a residual, if any, assigned to owners’ equity.

**Performance Reporting and Cash Flows**

We support the Board’s efforts to improve the usefulness of the information provided in an entity’s financial statements and to help users make decisions in their capacity as capital providers. We agree with many of the ITC’s perceived issues related to reporting performance and cash flows and believe them to be, collectively, a major reporting issue that the Board should consider improving. Another potential benefit of addressing performance reporting issues is that it can alleviate pressure on other issues. For example, where to present measurement changes may affect support for a particular measurement the Board is considering.

We believe that a comprehensive project to address performance reporting and cash flow issues, together, is warranted. Even if the Board decides not to address the issues comprehensively, narrower projects related to this topic may still be beneficial, such as addressing performance reporting issues connected with distinguishing liabilities from equity as discussed elsewhere in this letter.

We especially encourage the Board, when contemplating changes to the current performance reporting model, to consider the recent increase in use of and requests for non-GAAP measures since recent trends seem to indicate that users are looking for different types of information than what is currently provided under US GAAP. By acknowledging these recent trends and understanding what users are requesting, the Board will be able to incorporate meaningful changes into the financial reporting model.

The paragraphs below outline, for the Board’s consideration, a performance reporting model which may be useful to users and could be practically implemented by preparers.

**Income Statement**

The objectives described in the ITC, which if addressed and implemented appropriately, should benefit users by improving the structure and display of the information reported within the performance statement.

We have our own thoughts on a potential structure for improving and displaying performance information. The performance reporting model we are proposing consists of four principles-based categories:

1. **Central operating activities** – This category would consist of the results of transfers with other parties (within the current period or accruals for future
transfers) that are related to the entity’s ongoing major or central operations. The term “transfers” is used to distinguish the items in this section from “remeasurements.” Remeasurements are discussed as a separate category below (except remeasurements associated with “trading activities” which would be part of central operating activities). Transfers is also used instead of exchanges to indicate that the activities in this category are not always reciprocal.

2. **Peripheral activities** – This category would consist of transfers with other parties that are not central to an entity’s operating activities (e.g., non-recurring transfers). For example, this section may include a transfer of equipment or factoring of trade receivables.

3. **Remeasurements and periodic allocations** – The items in this category do not directly result from transfers. Such items would include gains and losses recognized as a result of the remeasurement (not the transfer) of assets and liabilities under GAAP. For example, a manufacturing entity may include within this category remeasurement gains and losses attributable to an equity investment measured at fair value. However, remeasurements related to assets or liabilities that are part of an entity’s trading operations that are part of its central operating activities would be classified in central operating activities, as discussed above. This section would also include allocations such as depreciation and amortization.

4. **Changes in non-owners’ equity** – All changes in assets and liabilities should be classified in one of the three categories above. Therefore, this category would solely consist of changes in non-owners’ equity (noted above) that are based on changes in the value of owners’ equity and time value and changes related to a non-controlling interest.

This performance reporting model would eliminate the need for a statement of other comprehensive income, which has been the subject of much confusion with financial statement users. However, certain additional complexities would need to be addressed. For example, the Board would need to address where there should be subtotals, particularly subtotals that are included in the numerator of earnings-per-share amounts. The Board may find that it needs to consider which remeasurements are above or below the subtotal used for earning-per-share (e.g., foreign currency translation adjustments, changes in the entity’s own credit related to debt measured at fair value). Another complication the Board will need to address is the model for cash flow hedges of forecasted transactions.

Such a performance reporting model would provide management the ability to classify an entity’s financial information on the basis of how the entity uses the underlying assets and liabilities rather than based on specific rules dictating the presentation. We realize that there may be certain practical concerns with such an approach, including potential difficulties in determining classification due to its subjective nature (i.e., two prudent individuals within the same entity looking at the same information could conclude differently). However, we believe the benefits of such an approach would outweigh its costs. We further propose that the Board address and potentially develop specific requirements for disclosures about the significant judgments an entity has made in determining the appropriate classification of its business activities into each of
the categories described above. Finally, the Board should address and potentially develop specific requirements for accounting for and disclosing changes in the category classification of items from one period to another.

We also support the idea that information in an entity’s financial statements should be disaggregated in enough detail to be decision-useful, particularly within a classification category that reflects the entity’s operating activities (such as the “central operating activities” classification proposed in the model described above). In addition to providing information that is useful in assessing future cash flows, certain disaggregation of information may also be useful in assessing past performance of management (i.e., management stewardship). However, because financial statements are prepared to provide a summarized view of an entity’s financial position and performance, we are concerned that too much disaggregation may distract users from relevant information and create a burden for preparers that may outweigh the potential benefits. The Board should consider additional analysis to determine the level of disaggregation users actually need and fully understand why such information is necessary before requiring entities to provide it in their financial statements. This analysis could also help the Board assess the costs and benefits of the principles behind this objective.

**Statement of Cash Flows**

We support the Board’s efforts to improve the usefulness of the statement of cash flows and acknowledge the challenges associated with the current model. The principles delineating operating, investing, and financing activities are not clear, intuitive, or conceptual, as demonstrated by the significant number of classification-related restatements that occur each year. We suggest that the Board reconsider the current three-category structure and propose a structure consistent with the performance statement model described above, which would provide consistent and cohesive performance reporting across the two statements. We believe cohesiveness among all financial statements and, especially, between the income statement and the statement of cash flows is important to enhance the usefulness of information provided to an entity’s stakeholders.

We recognize that providing an articulation or cohesiveness between the performance statement and statement of cash flows will likely require using the direct method to present cash flows. This may provide additional benefits as such a presentation would provide helpful information to financial statement users and would likely result in fewer misstatements than the indirect method. While we understand that historically the cost to change from the indirect method to the direct method of presenting cash flows has been a challenge, the Board should consider researching whether recent technological advances will now enable entities to change methods without incurring significant costs.

**Other Projects**

As noted above, we think the Board needs to be selective in deciding what to add to its current agenda. We would not recommend adding a project on pensions and other postretirement benefits. While the accounting model could certainly be improved, we believe that the current guidance is well understood by preparers, practitioners, and users and that the future benefits of significant amendments may
be limited. As for a project on intangible assets, we believe that the improvements the Board could currently make in this area are significantly limited and that given its limited resources, the Board could make more of an impact by working on the projects discussed above. If the Board was to add a project on intangible assets, we think an approach that leverages the work already performed by the IASB makes the most sense.

We also considered other potential projects that are not discussed in the ITC. Specifically, two issues we considered proposing to the Board are variable consideration and control. These two issues are cross-cutting in nature in that they affect several topics in the Codification. They are addressed differently in different topics, or not at all in some topics which creates confusion and unnecessary complexity.

We also considered a potential project on simplifying the consolidation guidance, particularly with respect to scope issues. We understand that the 2015 FASAC survey identified consolidation as a major area of financial reporting that warrants improvement. Further, we understand that the FASB decided not to include this topic in the ITC, because it recently added to its agenda a research project to potentially reorganize and clarify the consolidation guidance in ASC 810, Consolidation. We support the FASB’s research project on consolidation and believe the Board could simplify the requirements by establishing a single consolidation model. Aligning the consolidation models for variable interest entities with that for other types of entities would eliminate inconsistencies and reduce unnecessary complexity for preparers and practitioners.

In closing, whatever projects the Board adds to its agenda, we hope the Board will coordinate and share considerations with the IASB. While we realize it is likely these will not be joint projects our hope is that there will be some convergence.

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The appendix below contains our responses to the ITC’s questions for respondents.

We appreciate the opportunity to comment on the ITC. If you have any questions about our comment letter, please feel free to contact Bob Uhl at (203) 761-3152.

Yours truly,

Deloitte & Touche LLP
Question 0.1: Are there major financial reporting issues that are not considered in this ITC that should be addressed by the FASB before any of the issues discussed in the ITC are addressed? What are the considerations or criteria that you used to identify these issues? Please describe any of those issues and your perspective about how the FASB should resolve the issues.

As indicated in the body of this letter, two issues we considered proposing to the Board are variable consideration and control. These two issues are cross-cutting in nature in that they affect several topics in the Codification. They are addressed differently in different topics, or not at all in some topics which creates confusion, and unnecessary complexity. We also considered a potential project on simplifying the consolidation guidance, particularly with respect to scope issues. However, we do not believe that either of these issues should take priority over those identified in the ITC, particularly distinguishing liabilities from equity and reporting performance and cash flows.

Question 0.2: What is your view about the priority of addressing the major financial reporting issues addressed in this ITC? In other words, is addressing one or more of the issues more critical than others? Please describe your assessment criteria and why you prioritized certain issues above others.

As indicated in the body of this letter, we believe that the FASB should only add two of the four topics in the ITC to its current agenda: distinguishing liabilities from equity and reporting performance and cash flows.

While the other financial reporting issues identified in the ITC certainly have merit, we think that the Board needs to be selective in deciding what to add to its current agenda. If too many major projects are on the Board’s agenda at the same time, its resources and focus could be diluted, in which case it could need additional time to complete projects and may not implement the best solutions. While the accounting model for pensions and other postretirement benefit plans could certainly be improved, we believe that the current guidance is well understood by preparers, practitioners, and users and that the future benefits of significant amendments may be limited. As for a project on intangible assets, we believe that the improvements the Board could currently make in this area are significantly limited and that, given its limited resources, the Board could make more of an impact by working on the projects we discuss above. Therefore, we would not recommend that the Board add to its agenda a project on either pensions and other postretirement benefits or intangible assets.

Question 0.3: Is it necessary to resolve one or more of the issues before resolving others? In other words, is the resolution of any of the issues dependent upon the resolution of one or more other issues? Please identify any of the projects that should be completed before others and why.

As noted in the body of this letter, we believe that there is an interrelationship between distinguishing liabilities from equity and performance reporting, since performance reporting may be the key to differentiating claims on assets. Specifically,
a primary purpose of differentiating liabilities from equity under the current regime is to recognize changes in liabilities, but not changes in equity, in an entity’s performance statement (i.e., comprehensive income). As indicated in our proposed model for performance reporting, changes in non-owners’ equity would be reported in the performance statement in a separate category titled “Changes in Non-owners’ Equity.” We believe that if these changes are presented in a separate category in the performance statement, some of the pressure related to determining whether an instrument is classified as a liability or equity would be alleviated.

Chapter 1 — Intangible Assets (Including Research and Development)

Question 1.1: Is the accounting for intangible assets (including research and development) a major financial reporting issue that the FASB should consider for improvement? Please explain why.

We agree with the ITC’s perceived issues and inconsistencies related to accounting for intangible assets. However, as discussed in the body of this letter, we do not believe that the Board should add a project on intangible assets to its current agenda. While the accounting guidance on intangible assets could certainly be improved, we believe that the timing is not right for a broad project on this topic and that the benefits of a narrow project are not as great as the potential benefits of other projects. We believe that the Board should dedicate its resources to topics that we deem higher priorities — namely, distinguishing liabilities from equity and reporting performance and cash flows.

Question 1.2: If yes, should the issue be addressed broadly for all intangible assets or should it first be addressed for a subset of intangibles (for example, research and development)? Please explain why.

As discussed in our response to Question 1.1, we do not believe that the Board should add a project on intangible assets to its current agenda. However, if the Board does decide to add this topic to its current agenda, we believe that it will be critical to determine the project’s scope, given the vast array of intangible assets and various issues that arise in connection with different classes of intangible assets. We therefore recommend that the FASB first explore the alternatives and issues as part of a more focused project addressing research and development.

Question 1.3: Which approach to addressing the issue is appropriate, considering the benefits and costs of each approach and why? If you recommend a recognition approach, please explain your view about (a) the threshold for recognizing the asset and (b) the measurement of the asset (cost or fair value). If you recommend a disclosure approach, please explain the disclosure objective and recommend what specific information should be disclosed. If you recommend an approach to adopt IAS 38, please explain any implementation concerns.

We believe that currently it is impracticable to measure all intangible assets at fair value on a recurring basis, since the costs of such an approach would not outweigh the benefits. Further, we do not believe that the ITC’s “Alternative C,” which focuses strictly on additional disclosures, would be optimal, since the recognition and measurement issues related to intangible assets would most likely still be present.
While adopting IAS 38\(^1\) or a cost-based approach may be appropriate alternatives, we believe that the solution to the perceived issues should be a principles-based approach that can be applied to other types of intangible assets when and if the Board decides to address those issues in the future.

**Question 1.4:** Recognition of an intangible asset if a threshold is met and measurement of that asset at fair value would likely result in (a) a gain in the period in which the asset initially is recognized and (b) gains or losses in each period for the change in the fair value of the asset. How should those initial and subsequent gains and losses be presented in the income statement?

See our response to Question 1.3.

**Chapter 2 — Pensions and Other Postretirement Benefit Plans**

**Question 2.1:** Is the accounting for pensions and other postretirement benefit plans a major financial reporting issue that the FASB should consider for improvement? Please explain why.

While we support the FASB’s efforts to improve aspects of U.S. GAAP, we believe that the accounting for pensions and other postretirement benefit plans should not take priority over the other financial reporting issues we discussed earlier in our response. We believe that the current guidance on this topic is well understood by preparers, practitioners, and users and that the future benefits of significant amendments may be limited. The Board should also consider deferring completion of a project related to changes in measurement and presentation under ASC 715\(^2\) until it completes its broader research project on financial performance, since the decisions in, and completion of, the project on financial performance reporting are likely to affect current and potential proposed amendments that have an impact on the accounting for pensions and other postretirement benefit plans. Further, we believe that the current disclosure requirements in ASC 715 permit users to understand much of the impact of delayed recognition when performing financial analysis and to address some of the comparability issues that arise on the basis of the accounting policy elections of reporting entities.

However, if the Board decides to add this topic to its current agenda, we believe that targeted improvements to the accounting for pensions and other postretirement benefit plans would be the best approach. Currently, ASC 715 allows entities to make accounting policy choices for certain aspects of pension accounting, such as timing of gain/loss recognition in earnings (i.e., immediate recognition vs. delayed recognition). In addition, ASC 715 prescribes certain accounting practices that differ from those in IAS 19.\(^3\) Such differences diminish the comparability and decision-usefulness for financial statement users. Therefore, we believe that making targeted improvements, such as eliminating delayed recognition in earnings, will help the Board meet its current broad objectives of simplification and convergence with IFRSs.

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\(^1\) IAS 38, *Intangible Assets.*


\(^3\) IAS 19, *Employee Benefits.*
Issue 1—Delayed Recognition (Smoothing) in Earnings

Question 2.2: Would Alternative A (see paragraphs 2.15–2.16) and/or Alternative B (see paragraphs 2.17–2.19) improve the usefulness of financial information provided to users and be operable?

We believe that if the Board proceeds with addressing the issues described in the ITC, Alternative B would improve the utility of financial information provided to users and be operable. Eliminating all smoothing and recognizing the measured changes immediately in the income statement would, for example, eliminate differences in the currently available accounting policy choices related to immediate or delayed recognition of actuarial gains/losses in earnings. This alternative would also eliminate the initial recognition of prior service cost in other comprehensive income and the subsequent amortization of these costs to earnings. The recognition of prior service cost or credit immediately in earnings would be analogous to the accounting for modifications made to share-based payment awards under ASC 718 in which incremental expense is immediately recognized for awards that have already vested at the time the modification occurs. Immediately recognizing these costs in the income statement would increase the comparability of financial statements, more closely align the accounting with IAS 19, and reflect the current economic cost of the defined benefit plan.

We acknowledge that this alternative would lead to a difference between the recognition of actuarial gains/losses under IAS 19 and that under ASC 715 (i.e., IAS 19 requires recognition of all actuarial gains/losses in other comprehensive income, with no amortization (recycling) to earnings), but we believe that immediate recognition of actuarial gains/losses in the income statement better reflects the current economic impact of a company’s defined benefit plans.

Question 2.3: If you support Alternative A (convergence with IAS 19), would you recommend any modifications to IAS 19 or would you expect any implementation issues? Please explain why.

As we stated in our response to Question 2.2, we believe that Alternative B is the best approach for improving the utility of financial information provided to users.

Question 2.4: Are there other approaches to consider for addressing the issue of delayed recognition in earnings? If so, please provide them in sufficient detail so that the FASB can consider your proposal(s). Please provide your rationale for why your proposal provides users of financial statements with more useful information.

We currently do not have any additional approaches or recommendations. As we stated in our response to Question 2.1, we believe that the Board should consider deferring completion of a project on changes to presentation under ASC 715 until it completes work on its broader research project on financial performance reporting.

Issue 2 — Measurement of Defined Benefit Obligation

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4 FASB Accounting Standards Codification Topic 718, Compensation — Stock Compensation.
Question 2.5: Is the current measurement of a defined benefit obligation appropriate? If not, what changes do you suggest and why (for example, what characteristics of plans are not adequately reflected in the current measurement of the benefit obligation)?

Discount Rate Assumptions for Measuring the Projected Benefit Obligation

If the Board proceeds with addressing measurement issues described in the agenda consultation, we believe that it should consider the development of the discount rate assumption for measuring the projected benefit obligation or accumulated projected benefit obligation. Under ASC 715, discount rates used to measure the benefit obligation currently are based on a settlement-rate framework in which companies select discount rates that will reflect the rates at which the benefit obligation can be effectively settled. By contrast, IAS 19 requires an entity to measure the present value of the obligation on the basis of high-quality corporate bond discount rates that reflect the time value of money but does not include an underlying principle for developing the assumption on the basis of settlement rates. If the Board is planning targeted improvements in this area, we would encourage it to consider converging the ASC 715 approach with the IAS 19 approach in a manner that reduces the differences between the two accounting frameworks with respect to developing this key assumption.

Hybrid Plans and Measurement of Cash Balance Plans With Variable or Fixed Interest Crediting Rates

In practice, we have not encountered frequent questions about hybrid plans and are not aware of significant issues with the current accounting for hybrid plans that constitute defined benefit plans under ASC 715. Similarly, we are not aware of pressing issues or significant diversity in practice related to the measurement of cash balances with variable or fixed interest-crediting rates.

Potential Path Forward

Question 2.6: What approach (that is, targeted improvements or comprehensive reassessment) would you recommend and why?

As we stated in our response to Question 2.1, we believe that targeted improvements to the accounting for pensions and other postretirement benefit plans would be appropriate if the Board decides to amend the current accounting requirements. Targeted improvements should improve convergence with IFRSs and address comparability issues.

Question 2.7: Are there other issues for pension and other postretirement benefit plan accounting that should be considered for improvement?

If the Board proceeds with improving the accounting for pension and other postretirement benefit plans, we would encourage it to consider the additional considerations described in our April 25, 2016, comment letters on the FASB’s proposed Accounting Standards Updates (ASUs) Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost and Changes to the Disclosure Requirements for Defined Benefit Plans.
Specifically, in our letter on the proposed ASU on improving the presentation of net periodic pension cost and net periodic postretirement benefit cost, we indicated our beliefs that (1) amortization of prior service cost or credit should be treated similarly to current service cost and should therefore be presented together with the current service cost component, (2) the Board should remove the proposed amendment that would require the interest cost component of net benefit cost to be presented outside of operating income, and (3) either (a) reporting entities should have the flexibility to adapt the capitalization of such costs to their manner of conducting business with their customers or (b) the Board should consider granting exceptions allowing entities in certain industries to continue to capitalize the components of net benefit cost consistently with their recovery of such costs from their customers.

In addition, in our comment letter on the FASB’s proposed ASU on changes to the disclosure requirements for defined benefit plans, we suggested that the Board consider requiring an entity to disclose its accounting policy for measuring the market-related value of plan assets at either fair value or calculated value, since users may be interested in this disclosure for comparability purposes. Further, IAS 19 requires disclosure of all significant actuarial assumptions, whereas ASC 715-20 requires disclosure of only specified assumptions. To promote convergence with IFRSs, we suggest that the FASB consider requiring disclosure of all significant actuarial assumptions used to determine the present value of the defined benefit obligation and net benefit costs in a manner similar to the requirement in paragraph 144 of IAS 19.

However, as we stated in our response to Question 2.1, we believe that the Board should consider deferring completion of a project related to changes to presentation under ASC 715 until it completes work on its broader research project on financial performance reporting.

Chapter 3 — Distinguishing Liabilities From Equity

Question 3.1: Is the accounting for distinguishing liabilities from equity a major financial reporting issue that the FASB should consider for improvement? Please explain why. In making your assessment, what criteria were used (for example, is the issue not sufficiently addressed in current GAAP, or is it addressed in a way that makes compliance costly or creates diversity in practice because the guidance is conceptually or economically flawed)?

Yes. As discussed the body of this letter, we believe that the accounting for distinguishing liabilities from equity is a major financial reporting issue that the FASB should add to its technical agenda.

Question 3.2: Is the issue of distinguishing between liabilities and equity a financial reporting issue that requires a holistic approach to resolve as opposed to targeted improvements? Please explain why.

Yes. We believe that one of the fundamental issues in the current guidance is the internal inconsistency between various models that create complexity and cause instruments with economically similar terms to be accounted for in different ways. It seems unlikely that such pervasive issues would be sufficiently addressed through
targeted improvements. Our observations of the Board’s discussions on targeted improvements over the past year, including the difficulty of refining the accounting for instruments with down-round protection, further supports the need for a holistic approach. Throughout those discussions, the modifications to accounting guidance have been addressed in the context of achieving a desired result (e.g., instruments with down-round features no longer being precluded from equity classification) rather than from the perspective of a principles-based approach. Given the existing complexity in various models, a principles-based approach seems to be the most effective way to resolve apparent contradictions across various subsections of the literature.

Question 3.3: Are there other alternatives for simple instruments that the FASB should consider for resolving the issue of distinguishing between liabilities and equity? If so, please provide the alternatives in sufficient detail such that the FASB can consider your proposal(s). Please provide your rationale for why your proposal provides users of financial statements with more useful information.

Please see the body of this letter, in which we discuss our proposal to classify instruments within three categories: (1) liabilities, (2) non-owners’ equity, and (3) owners’ equity.

Question 3.4: Are there other alternatives for addressing the financial reporting issues with conversion options in complex instruments that the FASB should consider? If so, please provide sufficient detail such that the FASB can consider your proposal(s). Please provide your rationale for why your proposal provides the users of financial statements with more useful information.

As we discuss in the body of this letter, we believe that presenting the various components of complex instruments separately will provide the most helpful information to users. As discussed above, an existing issue with applying current GAAP on distinguishing liabilities from equity is that instruments with economically similar terms are accounted for differently as a result of their legal form. Separating the components of complex instruments would make the terms and features of these instruments clearer and more transparent for financial statement users. This approach is more consistent with the Board’s Alternative A proposal for complex instruments.

Question 3.5: Considering the alternatives described for simple instruments, which alternative provides more useful information to the users of financial statements and why?

Please see our proposal for three classes of instruments representing claims of the entity in the body of this letter. We support the Board’s proposal to require liability classification for instruments for which assets must be sacrificed before an entity’s liquidation. We also support separate classes for equity with the changes due to remeasurement of certain equity instruments recognized in comprehensive income.

Question 3.6: Considering the alternatives described for complex instruments, which alternative provides more useful information to users of financial statements and why?
As discussed in Question 3.4 above, the approach described in the body of this letter is more consistent with the Board’s Alternative A proposal for complex instruments, which we believe would provide more helpful information to users of the financial statements.

*Question 3.7: Which provides more useful information to the user of financial statements: remeasuring liability classified instruments at fair value or at intrinsic value? Please provide the rationale for your choice.*

We recognize that remeasurement is a critical issue in this project. We believe the Board needs to further analyze the presentation of changes resulting from remeasurement as well as what is the most appropriate measurement.

*Question 3.8: Are there instances in which the remeasurement of liability-classified instruments at each reporting period is not useful? If so, which instances and why?*

Please see our proposal for three classes of instruments representing claims of the entity in the body of this letter. We believe that financial statement users would find it beneficial to receive information on (1) the remeasurement of liability-classified claims and (2) the change in the measurement of instruments that would be classified in the non-owners’ equity category under our proposed model. For example, if a warrant is not liability-classified but would be classified in non-owners’ equity, we believe that it would be useful to understand the change in value so that equity owners can identify the potential value that would be reallocated to the warrant holders upon exercise of the warrant.

**Chapter 4 — Reporting Performance and Cash Flows**

We agree with many of the ITC’s perceived issues related to reporting performance and cash flows and believe them to be, collectively, a major reporting issue that the Board should consider for improvement. Therefore, we believe a comprehensive project to address the issues is warranted, as discussed in the body of this letter.

In our responses to the questions below, we discuss issues that we believe are essential to the development of a financial statement presentation model that provides helpful information for users and can be practically implemented by preparers.

**Income Statement**

*Question 4.1: Is income statement presentation a major financial reporting issue that the FASB should consider for improvement? Please explain why. In making your assessment, what criteria were used?*

Yes. As described above, we agree with many of the ITC’s perceived issues related to income statement presentation and believe them to be a major reporting issue that the Board should consider for improvement. In particular, we think that the Board should contemplate potential changes to the current financial reporting model given the recent increase in use of and requests for non-GAAP measures. Recent trends seem to indicate that users are looking for different types of information than what is currently provided under U.S. GAAP, and preparers are facing increasing pressures to present financial reporting information in various formats that may or may not
conform to current guidance.

Question 4.2: How should the components of net income be categorized, if at all? If the FASB were to develop an operating activities category and display a subtotal for operating income, how should the category be defined or described?

Please see our previous discussion on this topic in the body of this letter.

Question 4.3: Could an operating activity category be defined or described consistently and effectively for all types of reporting entities (for example, entities involved in financial services, investing, banking, and financing)?

Please see our previous discussion on this topic in the body of this letter with respect to a classification such as “central operating activities.” We believe that the standard should contain a principle or objective that entities would apply to their particular facts and whose application would be disclosed. Although such a principle or objective could create some diversity in practice, it would be useful to understand an entity’s views on what its central and ongoing operations are.

Question 4.4: How should the FASB evaluate the benefits of a standardized definition versus a management determination of an entity’s operating activities?

As described in the body of this letter, we believe that a principles-based model for income statement classification is essential to enhancing the usefulness of the income statement for stakeholders. A model such as the one described in the body of this letter would allow management to classify an entity’s financial information on the basis of how the underlying assets and liabilities are used by the particular entity, as opposed to employing a presentation based on specific rules, which may or may not provide useful information to stakeholders. Under such an approach, for example, information on the way an entity primarily creates value (i.e., its central business activities) could be presented separately from information on how it funds those activities (i.e., its financing activities). Such a presentation may be clearer for financial statement users.

Question 4.5: Which, if any, of the three alternatives described for combining or separating items provides more useful information to users of financial statements, and why?

Please see our previous discussion on this topic in the body of this letter.

Question 4.6: Are there other alternatives for presenting lines within the income statement that the FASB should consider?

Please see our previous discussion on this topic in the body of this letter.

Segment Reporting

Question 4.7: Is segment disclosure a major financial reporting issue that the FASB should consider for improvement? In making your assessment, what criteria were used?
The SEC has focused on segment reporting for many years, and this topic has therefore been a concern for many companies. However, we do not recommend that the FASB take on a broad project related to the segment standard at this time. Nevertheless, we believe that the Board could reduce some of the perceived issues related to segments if the quantitative thresholds in ASC 280-10-50-12 precede the aggregation criteria in ASC 280-10-50-11. Applying a quantitative threshold before the aggregation criteria would increase transparency for financial statement users and may make it easier for preparers to apply the standard.

**Question 4.8:** Considering the three alternatives described for improving aspects of the Topic 280 disclosure requirements, which, if any, alternative provides more useful information to the users of financial statements and why?

The current segment standard is from management’s perspective, and the alternatives presented are in line with that approach. Entities may assert that the chief operating decision maker does not regularly review many of the items shown in the three disclosure alternatives and thus would not be required to disclose those items. Therefore, the additional disclosure requirements in the three alternatives would not result in more helpful information for financial statement users.

**Question 4.9:** Would the described improvements to (a) reexamine the aggregation criteria and (b) apply the segment standard from a governance perspective provide more useful information to users of financial statements and why?

No, we do not believe that these described improvements would provide more helpful information to financial statement users. The application of the segment standard from a governance perspective would most likely result in fewer operating and reportable segments and would be inconsistent with the standard’s objective.

**Question 4.10:** Are there other alternatives for improving segment reporting that the FASB should consider? If so, please provide them in detail to help the FASB in considering your proposal(s). Please provide your rationale for why your proposal provides users of financial statements with more useful information.

Yes. See our response to Question 4.7.

**Other Comprehensive Income**

**Question 4.11:** Is the presentation of other comprehensive income a major financial reporting issue that the FASB should consider for improvement? In making your assessment, what criteria were used?

Yes. We understand that many users believe the current presentation of other comprehensive income to be unclear and therefore do not find such information particularly relevant. The primary issue is that there is no conceptual basis for defining other comprehensive income, and we are skeptical that one could be developed. Of particular concern is the determination of whether some changes in assets and liabilities (and potentially equity) should be excluded from a “net income” subtotal and from the numerator in earnings-per-share. As noted in the body of our letter, the Board should focus on what items are included in the subtotal and earnings-per-share.
Question 4.12: Considering the two alternatives described for minimizing the use of reclassification adjustments, which alternative provides more useful information to the users of financial statements and why?

Please see our previous discussion in the body of this letter. If the Board adopts a model similar to the one we have proposed, other comprehensive income would be eliminated. While our model still allows for flexibility in presenting certain changes below a “net income” subtotal and outside of earnings-per-share, it would generally eliminate reclassification adjustments. We encourage the Board to seek input from financial statement users regarding the alternative that provides the most useful information.

Question 4.13: Do the described improvements to (a) remove the option for presenting comprehensive income over two statements and (b) emphasize other earnings per share measures improve the relevance of the performance information included in other comprehensive income?

Please see our previous discussion in the body of this letter. If the Board adopts a model similar to the one we have proposed, other comprehensive income would be eliminated. We encourage the Board to seek input from financial statement users regarding the alternative that provides the most useful information.

Question 4.14: Are there other alternatives for improving the relevance of other comprehensive income that the FASB should consider? If so, please describe them in detail to help the FASB in considering your proposal(s). Please provide your rationale for why your proposal provides users of financial statements with more useful information.

Please see our previous discussion on this topic in the body of this letter.

Cash Flow Statement

Question 4.15: Is the presentation of cash flows a major financial reporting issue that the FASB should consider for improvement? In making your assessment, what criteria were used?

Yes. As described above, we agree with many of the ITC’s perceived issues related to the cash flow statement and believe them to be a major reporting issue that the Board should consider for improvement, especially given the high number of financial statement misstatements related to the cash flow statement. As noted above, we recommend a comprehensive project that would create consistency among all financial statements, particularly between the statements of comprehensive income and cash flows.

Question 4.16: Do you recommend that the FASB retain or reconsider the three-category structure and the definitions of operating, investing, and financing activities within the statement of cash flows?

Please see our previous discussion on this topic in the body of this letter, in which we recommend changing the structure of the cash flow statement and replacing the
current three-category structure. Regardless of the structure and definitions that the Board ultimately determines should be used with respect to the cash flow statement, we believe it is critical that the structure and categories be consistent with those for the other financial statements, especially the statement of comprehensive income. Such consistency is critical to users’ understanding of the historical performance in terms of both income and cash flows and to providing information with the predictive value desired by users.

**If the FASB Maintains the Current Three-Category Structure and Definitions**

**Question 4.17: What specific cash flows should be disaggregated in the future that are not being disaggregated today and is that disaggregation feasible?**

As stated above, we support the idea that when information in an entity’s financial statements is disaggregated, it should contain enough detail to be decision-useful, particularly when the information is in a classification category that reflects the entity’s operating activities (such as the "central operating activities" classification proposed in the model described above). However, we believe the Board should attempt to determine the level of disaggregation users actually need and to fully understand why such information is necessary before requiring it in entity’s financial statements. This analysis could also help the Board assess the costs and benefits of the principles behind this objective.

**Question 4.18: What specific cash payments and receipts are in need of additional classification guidance?**

As noted in Question 4.15, we believe that the Board should embark on a comprehensive project to holistically address the cash flow statement. However, in the short term, if the Board wishes to eliminate the current diversity in practice related to the existing cash flow classification guidance, it appears that narrow-scope projects (such as the recent EITF projects related to Issues 15-F and 16-A), particularly those associated with cash payments and receipts in the operating activities category (where the most aggregation seems to occur), are the best alternative.

**If the FASB Reconsiders the Current Three-Category Structure and Definitions**

**Question 4.19: How should the cash flow statement be categorized, if at all? Considering the three alternatives that would reconsider the current structure of the cash flow statement, which, if any, alternative provides more useful information to users of financial statements and why? How should the FASB define or describe those categories?**

Please see our previous discussion on this topic in the body of this letter.

**Question 4.20: How should the FASB evaluate the benefits of a standardized structure versus a management determination to classification of cash flows?**

Consistent with our response to Question 4.4, we believe that a principles-based model for cash flow statement classification is essential to enhancing the usefulness of the cash flow statement for stakeholders. Such a model would allow management
to classify an entity’s cash flows on the basis of how the cash was received or used, as opposed to employing a presentation based on specific rules, which may or may not provide useful information to stakeholders. Under such an approach, for example, information on the primary way an entity generates cash (i.e., through its central business activities) could be presented separately from the way it funds its activities (i.e., its financing-related cash flows). Such a presentation may be clearer for financial statement users.

Question 4.21: If you prioritize a standardized structure and recommend an operating activities category, how should the Board evaluate the benefits of aligning the description or definition of that category across the income and cash flow statements?

Please see our previous discussion on this topic in the body of this letter. Also see our answers to previous questions in which we express our view that regardless of the classification rules that may ultimately be prescribed, consistency between the income statement and the cash flow statement is vital.

Question 4.22: Are there other alternatives for improving the cash flow statement that the FASB should consider? If so, please describe in detail to help the FASB consider your proposal(s). Please provide your rationale for why your proposal provides users of financial statements with more useful information.

Please see our previous discussion on requiring the use of the direct method in the body of this letter.

Paths Forward

Question 4.23: What type of project or projects do you recommend that the FASB prioritize to improve the reporting of performance and cash flow information? If you recommend multiple projects or different combinations, please explain the recommended sequencing of those projects.

As noted in the body of this letter, we agree with many of the ITC’s perceived issues related to reporting performance and cash flows and believe them to be, collectively, a major reporting issue that the Board should consider for improvement. Therefore, we believe that a comprehensive project to address the issues is warranted and that it should result in a financial reporting model that promotes consistency in classification among the various financial statements. We acknowledge that a comprehensive and holistic project to improve performance reporting in the manner in which we have proposed would be a long-term project. Therefore, as we note in our response to Question 4.18 with respect to the cash flow statement, if the Board wishes to eliminate current diversity in practice related to performance reporting in the short term, it may need to continue to identify and complete narrow-scope projects.

Question 4.24: What issues and solutions should be addressed within those projects? Please consider the priority of pursuing the issues and solutions.

Please see our previous discussion in the body of this letter containing our comments on elements we believe to be essential to the development of a financial statement
presentation model that provides useful information for users and can be practically implemented by preparers.